QUESTION PRESENTED

The United States will address the following question:

Whether a recipient of nonpublic information concerning ongoing criminal conduct within a corporation violates the antifraud provisions of the federal securities laws by transmitting that information to other persons, including persons who may use it in making investment decisions, when the recipient of the information has no fiduciary relationship with the securityholders of the corporation and there is no element of misappropriation in transmitting or utilizing the information.

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In the Supreme Court of the United States

OCTOBER TERM, 1982

No. 82-276

RAYMOND L. DIRKS, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE IN SUPPORT OF REVERSAL

INTEREST OF THE UNITED STATES

The court of appeals has affirmed an order of the Securities and Exchange Commission censuring petitioner for violating the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), based on his transmittal of nonpublic information concerning an ongoing corporate crime. The United States and the Commission share enforcement responsibilities under Section 10(b) and Section 17(a). See 15 U.S.C. 77t(b), 78*o*(b)(4), 78u(d), 78aa and 78ff. The United States therefore has an interest in the correct interpretation of the antifraud provisions at issue in this case. See *Chiarella* v. *United States*, 445 U.S. 222 (1980).

As reflected in their past enforcement activities, the United States and the Commission are in general agree-

ment about the scope and application of the antifraud provisions. The disagreement in the present case is a narrow one. It arises from the Commission's application of the well-established rule against tipping inside information to petitioner's dissemination of evidence of crime. In the view of the United States, the Commission's order censuring petitioner cannot be reconciled with this Court's decision in *Chiarella* v. *United States*, *supra*, and threatens to impair private initiative in uncovering violations of federal law.

STATEMENT

Petitioner Dirks is a securities analyst, "well-known for his investigative talents," who researched insurance company securities (Pet. App. B-3). In March 1973, petitioner applied those investigative talents to uncover a major fraud perpetrated by the officers of a publicly-owned insurance company. As the court of appeals observed, "in two weeks of concerted effort, at times resembling something from detective fiction, Dirks investigated and confirmed rumors of massive fraud by the Equity Funding Corporation of America (Equity Funding), an insurance holding company whose stock traded on the New York Stock Exchange. Largely thanks to Dirks one of the most infamous frauds in recent memory was uncovered and exposed * * *" (Pet. App. A-3; footnote omitted). Despite his efforts to uncover and expose the criminal scheme at Equity Funding, the Securities and Exchange Commission charged petitioner with "tipping" material inside information in violation of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a). Following an administrative hearing, the Commission entered an order finding petitioner to be in violation of those provisions (Pet. App. B-1 to B-27) and the court of appeals affirmed (Pet. App. A-1 to A-41).

1. Petitioner first learned of the fraud at Equity Funding from a former officer of the company, Ronald Secrist, who met with him for several hours on March 7, 1973. "Secrist made a series of detailed but nearly incredible allegations about Equity Funding" (Pet. App. A-5), including allegations that the company had produced large numbers of spurious insurance policies to inflate its sales revenues and that "its top officers had Mafia connections which they used to threaten the lives of employees who objected to the fabrications" (*ibid.*; Pet. App. B-3 to B-5 & n.8). Secrist urged petitioner to verify the existence of the fraud and then expose it (J.A. 14-15). He expected petitioner to transmit evidence of the fraud to "his firm's customers" and "clients" (J.A. 25), thereby triggering large-volume securities sales that would lead to a full investigation: "by jarring the stock, he would jar the corporat[ion]—this was my plan—he would jar the corporate officers and would also rattle the Wall Street financial community to the extent that someone would take action very quickly" (J.A. 16). Secrist believed that selling pressure would cause the price of Equity Funding stock to "drop close to zero very quickly" (*id.* at 26-27), and thus "reveal the fraud to the world" and "prevent its continuation" (*id.* at 27, 258).

During their initial meeting, petitioner sought and obtained Secrist's permission to convey evidence of the fraud to the *Wall Street Journal* (J.A. 22, 27-28, 37-38). Secrist warned, however, that merely presenting the information to regulatory authorities, including the SEC, would be abortive (J.A. 15-16, 36-37; Pet. App. B-4). Secrist stated that employees who attempted to do this in the past had been "brushed aside with a comment that that's a ridiculous story" (J.A. 16); those employees also found that the information was sometimes relayed back to Equity Funding and that "they were placed in personal jeopardy as a result of having gone there" (J.A. 22-25, 36-38, 66-67, 229; Pet. App. A-9 to A-10 n.6, B-4 to B-5 n.8).

Petitioner commenced his investigation by examining publicly available financial data and by contacting other members of the investment community to see if they had learned of the fraud allegations (Pet. App. A-5; J.A. 71-72). This inquiry proved fruitless. Petitioner then decided to personally investigate the allegations by flying from New York to Los Angeles to interview present and former employees of Equity Funding (Pet. App. A-6). Despite repeated denials of wrongdoing by the company's senior management (*ibid.*; J.A. 237-238), petitioner obtained substantial corroboration of the charges of fraud from one current and six former Equity Funding employees (Pet. App. B-9).

Throughout his investigation, petitioner spoke with a number of investors and analysts—"some because he hoped they might give him information or support, others because they were clients or potential clients and his records showed they were interested in information about Equity Funding, and still others simply because, having heard rumors about his investigation, they called him" (Pet. App. A-7; J.A. 71-72, 245-246). Not surprisingly, some of the persons who spoke with petitioner and learned of the alleged fraud sold their holdings of Equity Funding securities. Five investment advisers who communicated with petitioner liquidated securities worth more than $16 million (Pet. App. A-8).

In addition to interviewing former employees of Equity Funding, petitioner also met with Equity Funding's present and former auditors in an attempt to spread word of the fraud and bring it to a halt. As the Commission explained (Pet. App. B-9 n.12):

> Dirks also learned that [Equity Funding's] auditors were about to release certified financial statements for the company on March 26. He immediately contacted them and apprised them of the fraud allegations, hoping that they would withhold release of their report and seek a halt in the trading of [Equity Funding] securities. Instead, the auditors * * *

> merely reported Dirks' allegations to [Equity Funding's] management.

While petitioner believed that his revelations to the auditors would lead to a trading halt by the "New York Stock Exchange" or "the SEC" (J.A. 42-46, 59, 243-244), neither the current nor the former auditors were able to achieve that result (J.A. 56-59).[1]

As early as March 12, 1973, petitioner also attempted to communicate his evidence to the *Wall Street Journal* (Pet. App. B-5; J.A. 47, 230). "Dirks expected that a highly respected publication like the *Wall Street Journal* could be effective in helping him investigate the Secrist allegations and to expose the * * * fraud if it proved to exist" (J.A. 233). Those efforts also were unavailing (J.A. 47-56, 59-62, 270-271). As the court of appeals explained (Pet. App. A-9):

> [D]uring the entire week that Dirks was in Los Angeles investigating Equity Funding, he was also in touch regularly with William Blundell, the *Wall Street Journal*'s Los Angeles bureau chief. Dirks kept Blundell up to date on the progress of the investigation and badgered him to write a story for the *Wall Street Journal* on the allegations of fraud at Equity Funding. Blundell, however, was afraid that publishing such damaging rumors supported only by hearsay from former employees might be libelous, so he declined to write the story.

Petitioner provided Blundell with "the substance of all he knew," including his "notes" and the "names" of all witnesses (J.A. 238). Nevertheless, given the "scope of the fraud," Blundell doubted that it could have been "missed by an honest auditor" and discounted the entire allegation (J.A. 123, 136).

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[1] While communicating with the auditors, petitioner concealed his whereabouts to protect his personal safety (J.A. 243-244). When he learned that the auditors had merely conveyed his accusations back to Equity Funding's management, petitioner fled his hotel room in a " 'state of panic' " (*id.* at 244).

Increasing circulation of rumors about the fraud led petitioner to believe that it was "unlikely that [Equity Funding] stock would open for trading on Monday, March 26, because * * * trading [would] be halted by the NYSE [New York Stock Exchange]" (J.A. 244).[2] This did not occur, however, and petitioner again spoke to William Blundell of the *Wall Street Journal* and urged him to publish a story exposing the fraud. Blundell refused to do so but stated that he intended to discuss the matter with the SEC's Los Angeles Regional Office. Blundell secured petitioner's permission to propose a meeting with the SEC that would include himself and two other key witnesses (J.A. 245, 270). Petitioner then contacted the SEC and voluntarily presented all of his information at the SEC's regional office beginning on March 27 and continuing throughout the next three days (Pet. App. A-10; J.A. 62, 245).

During the two-week period in which petitioner pursued his investigation and spread word of Secrist's charges, the price of Equity Funding stock fell precipitously from $26 per share to less than $15 (Pet. App. A-10). This led the New York Stock Exchange to halt trading in the stock on March 27 (*ibid.*). Shortly thereafter, Illinois and California insurance authorities impounded Equity Funding's records and uncovered evidence of the fraud (Pet. App. A-11). Only then did the SEC file a complaint against Equity Funding and only then did the *Wall Street Journal* publish "a front page story written by Blundell but based largely on information assembled by Dirks" (Pet. App. A-11; J.A. 270-271). Three days later, Equity Funding filed a petition under Chapter X of the Bankruptcy Act (J.A. 5).

While petitioner's investigative activities succeeded in revealing in a few days that " 'one of the darlings of

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[2] As early as March 19, Secrist informed petitioner that he had reported his allegations to both state insurance regulators and the SEC. Despite his reservations about the regulators, Secrist believed that they too might take action. J.A. 50-51.

Wall Street, a company that had managed to produce continued high earnings growth for a decade, * * * was, instead, a gigantic fraud'" (Pet. App. B-22; footnote omitted), government authorities with jurisdiction over Equity Funding did not move so quickly (Pet. App. A-3).[3] As early as 1971, the SEC had received allegations of fraudulent accounting practices at Equity Funding (Pet. App. A-9 n.6; J.A. 100-114, 160-162, 270 n.49). Moreover, on March 9, 1973, an official of the California Insurance Department informed the SEC's regional office in Los Angeles of Secrist's charges of fraud (Pet. App. A-10 n.6, B-11 n.18; J.A. 91-99, 171-172, 269). The SEC's staff attorney "stated that similar allegations had been made about Equity Funding before by disgruntled employees." He nonetheless recommended "'delaying any type of inspection of the Equity Funding operations until next year * * *'" absent further corroboration (Pet. App. A-10 n.6; J.A. 95-99, 171-172). Equity Funding's Chairman—one of the principal architects of the fraud—testified that, prior to March 1973, he received no questions from auditors, state regulatory authorities, or federal regulatory authorities that suggested "they suspected there was a fraud at Equity Funding" (J.A. 116-117). When asked whether petitioner was "personally responsible for having uncovered the events at Equity Funding," he candidly stated: "I think Mr. Dirks is entitled to personal credit for that" (J.A. 115).

Following public revelation of the Equity Funding scandal, a federal grand jury in Los Angeles returned a 105 count indictment against 22 persons, including many of Equity Funding's officers and directors, alleging violations of the antifraud provisions of the federal securities laws, mail fraud, bank fraud, interstate trans-

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[3] Equity Funding had made "bogus entries in its books since 1964" (Pet. App. B-11). Of the more than $3 billion worth of life insurance ostensibly issued by Equity Funding after that time, more than $2 billion proved to be fictitious (*id.* at B-11 n.19).

portation of counterfeit securities, interstate transportation of securities obtained by fraud, and other federal felonies. Those proceedings were concluded by entry of guilty pleas or convictions after trial of all defendants for one or more of the counts against them (J.A. 5-6). Equity Funding's Chairman, Stanley Goldblum, received an eight-year prison sentence and a substantial fine (J.A. 151).

2. While the *Wall Street Journal's* reporter, William Blundell, was "nominated for a Pulitzer Prize for his coverage of the Equity Funding scandal" (Pet. App. A-11; footnote omitted), petitioner was charged by the SEC with violating the antifraud provisions of the federal securities laws based on his selective revelation of information about Equity Funding prior to general public disclosure. Following an administrative hearing, the Commission found that petitioner had "tipped" nonpublic information concerning Equity Funding in violation of those provisions. It observed that "Dirks received the information from inside corporate sources. From the nature of the information, the inference must have been obvious that his sources had received it during the course of their corporate duties, and that the company intended that it should be kept in confidence" (Pet. App. B-20; footnote omitted). The Commission added (Pet. App. B-21 n.42) that

> In tipping potential traders, Dirks breached a duty which he had assumed as a result of knowingly receiving confidential information from [Equity Funding] insiders. * * * Such a tippee breaches the fiduciary duty which he assumes from the insider when the tippee k owingly transmits the information to someone who will probably trade on the basis thereof.

The Commission reached that conclusion even though it recognized that "Dirks' informants were entitled to disclose the [Equity Funding] fraud in order to bring it to light and its perpetrators to justice" (*ibid.*).

Despite its finding of a violation, the Commission imposed only a censure—its mildest sanction—on petitioner. It observed that "it is clear that Dirks played an important role in bringing [Equity Funding's] massive fraud to light, and [that] * * * he reported the fraud allegations to [Equity Funding's] auditors and sought to have the information published in *The Wall Street Journal*" (Pet. App. B-26).

3. The court of appeals affirmed the Commission's censure order by a divided vote (Pet. App. A-1 to A-41). The court recognized both that there is "good reason to release corporate employees from their duty to keep corporate information confidential when the information concerns corporate crimes" (Pet. App. A-25), and that there is a weighty public interest in encouraging private persons to uncover evidence of criminal conduct (*id.* at A-25 to A-26; footnotes omitted):

> Both the state and the public at large have an interest in exposing corporate misconduct. Ordinarily, we would expect that official law enforcement agencies would be sufficient for that task, but this case shows that the organs of government are not always able to accomplish swift investigation of possible crimes. The press also has an historic role in discovering and exposing wrongdoing, but here, too, the press failed to move as quickly as Dirks, who had more immediate financial and reputational incentives to discover the truth about Equity Funding. Interpreting Rule 10b-5 so as to categorically prevent private sector investigators from contacting corporate employees and asking them about crimes or frauds that their employer is committing may not, in the end, serve the public interest.

Despite this concern, the court held that petitioner had engaged in fraudulent tipping in violation of the securities laws. The court concluded that since corporate employees could not themselves trade in Equity Funding securities without disclosing all material nonpublic in-

formation in their possession, petitioner was under an identical disability. The court believed that "the obligations of corporate fiduciaries pass to all those to whom they disclose their information before it has been disseminated to the public at large" (Pet. App. A-25). Thus, the court reasoned, petitioner was under a duty to make full public disclosure of his information or abstain from trading or tipping (*id.* at A-21).

INTRODUCTION AND SUMMARY OF ARGUMENT

1. This Court's recent decision in *Chiarella* v. *United States*, 445 U.S. 222, 231 (1980), establishes that the antifraud provisions of the federal securities laws forbid nondisclosure of information only when there is an "affirmative duty" to make disclosure. Congress has not enacted a "parity-of-information" requirement under these statutes (*id.* at 233), and policy arguments based on "unfairness" do not substitute for a duty to disclose that is rooted in legal principle (*id.* at 232).

The Justices of this Court unanimously agreed in *Chiarella* that there is no general duty to make disclosure before trading with or tipping material nonpublic information. Instead, such a duty arises either from the existence of a fiduciary relationship between the defendant and uninformed investors, or some act of misappropriation or conversion. See 445 U.S. at 228-235; *id.* at 238-239 (Brennan, J., concurring); *id.* at 239-245 (Burger, C.J., dissenting); *id.* at 245-247 (Blackmun, J., dissenting).

2. These principles establish that petitioner had no duty to disclose or abstain from trading or tipping. He was not a fiduciary with respect to the securityholders of Equity Funding. To the contrary, he was a complete stranger to those investors: he took no action, directly or indirectly, that would induce them to repose trust or confidence in him. Moreover, no ground exists for classifying him as a constructive fiduciary *ex malefico*. He engaged in no tortious or dishonest conduct that would

justify the imposition upon him of the obligations of a constructive trustee.

Similarly, there is no basis for concluding that petitioner misappropriated confidential information or participated in a breach of fiduciary duty, misconduct that gives rise to a duty of full disclosure. As both the Commission and the court of appeals recognized, petitioner's informants acted lawfully when they imparted their information to him, and petitioner used that information in precisely the manner that his informants expected.

3. The Commission's erroneous imposition of liability in this case has serious consequences for federal law enforcement, which frequently depends on private initiative to uncover criminal conduct. If the antifraud provisions of the federal securities laws, backed by administrative, civil, and criminal sanctions, forbid analysts to trade with or transmit evidence of crime obtained through honest investigation, then few analysts will have an incentive to invest the resources needed to investigate corporate frauds like the Equity Funding fraud. Few analysts will be willing to devote substantial resources and expose themselves to personal danger to investigate rumors of crime—as petitioner did—if they are forbidden to utilize the information they obtain until after it is fully revealed to the investing public.

Considerations of investor confidence and fairness, which have great weight in traditional insider trading cases, do not support the imposition of liability here. Petitioner's investigative activities brought to a halt a massive fraud that had victimized investors for nearly a decade, and which could have persisted undetected for many years to come. Petitioner accomplished what regulatory authorities were unable to do. Deterrence of such investigative action in the future will diminish, not increase, the confidence of the investing public. Moreover, while considerations of fairness preclude those with privileged access to confidential information from exploiting that advantage in violation of fiduciary duty, the

information obtained by petitioner was "secured by the private initiative of someone who enjoyed no privileged position with respect to access to information." Lorie, *Insider Trading: Rule 10b-5, Disclosure, and Corporate Privacy: A Comment*, 9 J. Legal Stud. 819, 821 (1980). Accordingly, there is no sound basis in policy for deterring analysts from exercising such private initiative in the future.

ARGUMENT

PETITIONER'S SELECTIVE TRANSMITTAL OF NONPUBLIC INFORMATION CONCERNING CRIMINAL CONDUCT AT EQUITY FUNDING WAS NOT FRAUDULENT BECAUSE PETITIONER HAD NO FIDUCIARY DUTY TO MAKE GENERAL DISCLOSURE TO SECURITYHOLDERS AND BECAUSE THERE WAS NO ELEMENT OF MISAPPROPRIATION IN TRANSMITTING OR UTILIZING THAT INFORMATION

The Commission and the court of appeals concluded that petitioner was subject to a duty to disclose to the public at large his evidence of criminal conduct or abstain from passing it on to anyone. The premise of that conclusion was that the sources of the information—present and former officers of Equity Funding—were subject to a fiduciary duty to the company's securityholders. The Commission believed that petitioner "assumed" that fiduciary duty simply by receiving the information, and that this prevented him from either tipping or trading (Pet. App. B-21 n.42). The court of appeals likewise believed that a fiduciary duty "pass[ed]" automatically to petitioner from his corporate informants (Pet. App. A-25).[4]

[4] The court of appeals articulated an alternative theory of liability based on petitioner's status as a registered broker-dealer, which the court believed to be sufficient to trigger a duty of general public disclosure (Pet. App. A-27 to A-31). That theory was not relied on by the Commission when it rendered its decision and is not relied on by the Commission in this Court as a ground for affirmance (Br. in Opp. 16). In these circumstances, there is no

In this Court, the Commission argues once again that petitioner "inherited" a fiduciary duty to Equity Funding's securityholders (Br. in Opp. 14-15). These verbal characterizations do not, however, establish an "affirmative duty to disclose" as required by *Chiarella* v. *United States*, 445 U.S. 222, 231 (1980). Moreover, treatment of petitioner's conduct as a form of fraudulent tipping threatens to significantly undermine the incentive of private persons to ferret out and reveal evidence of crime.

I. Failure To Publicly Disclose Information Before Selectively Transmitting It Or Engaging In Securities Transactions Based Upon It Is Not Fraudulent Unless There Is An Affirmative Duty To Make General Public Disclosure

1. The antifraud provisions involved in this case, Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), are key components of the government's "arsenal of flexible enforcement powers." *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 195 (1976).[5] Section 17(a) is broadly phrased "to protect against fraud and promote the free flow of information in the public dissemination of securities." *Rubin* v. *United States*, 449 U.S. 424, 431 (1981). It therefore serves to

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need for the Court to consider this alternative theory of liability (see *SEC* v. *Chenery Corp.*, 332 U.S. 194, 196 (1947)), and we do not address it in this brief.

[5] Although Section 10(b) and Section 17(a) both extend to a wide variety of fraudulent practices, there are certain differences in their coverage. See, e.g., *Aaron* v. *SEC*, 446 U.S. 680, 687-702 (1980). In determining whether there is a duty to disclose nonpublic information before trading or tipping, however, identical principles apply. Neither the Commission nor the court of appeals identified any difference between the antifraud provisions that is relevant in this respect, and the language of the provisions does not suggest any relevant difference. See Brudney, *Insiders, Outsiders, and Informational Advantages Under the Federal Securities Laws*, 93 Harv. L. Rev. 322, 324-325 n.17 (1979).

insure "'a high standard of business ethics'" in every facet of the securities industry. *United States* v. *Naftalin*, 441 U.S. 768, 775 (1979). Similarly, Section 10(b) is a "'catchall'" provision aimed at all types of fraudulent securities practices (*Ernst & Ernst* v. *Hochfelder*, *supra*, 425 U.S. at 203), which is to be construed "'not technically and restrictively, but flexibly to effectuate its remedial purposes'" (*Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 151 (1972)).

These comprehensive antifraud provisions condemn not only false statements and partial truths in connection with securities transactions, but also failures to disclose material nonpublic information when there is a duty to disclose. "Thus, administrative and judicial interpretations have established that silence in connection with the purchase or sale of securities may operate as a fraud * * * despite the absence of statutory language or legislative history specifically addressing the legality of nondisclosure." *Chiarella* v. *United States*, 445 U.S. 222, 230 (1980). In particular, it is well settled that "a corporate insider must abstain from trading in the shares of his corporation unless he has first disclosed all material inside information known to him." *Id.* at 227. In addition, "[t]ippees" who trade with information obtained from corporate insiders are liable under the antifraud provisions "because they have a duty not to profit from the use of inside information that they know is confidential and know or should know came from a corporate insider * * *." *Id.* at 230 n.12. As the Commission correctly explained (Pet. App. B-13 to B-14; footnote omitted), "[w]here 'tippees'—regardless of their motivation or occupation—come into possession of material 'corporate information that they know is confidential and know or should know came from a corporate insider,' they must either publicly disclose that information or refrain from trading. In addition, under aiding and abetting principles, a non-trading tipper is liable where he knew

or should have known that his tippee would be likely to trade."[6]

2. As this Court has made clear, however, liability for nondisclosure of nonpublic information is not without limitation. As a general proposition, there is no duty to disclose information to the public at large before engaging in a commercial transaction or before imparting the information to other persons. Thus, "one who fails to disclose material information prior to the consummation of a transaction commits fraud only when he is under a duty to do so." *Chiarella* v. *United States*, *supra*, 445 U.S. at 228. This Court's decision in *Chiarella*, which reviewed the law applicable to both "inside information" cases (*id.* at 226-230) and "market information" cases (*id.* at 231-235), delineates the circumstances in which there is a duty to disclose.[7]

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[6] Although the Commission and the United States disagree about the proper application of these general principles to the facts of this case—involving the selective dissemination of evidence of crime—there is no disagreement about the legal principles themselves. Insiders, outsiders, and their tippees who misuse material confidential information in securities transactions are subject to both civil and criminal liability under the federal securities laws. In particular, corporations that issue securities, their insiders, and tippees may not trade with or selectively disseminate confidential inside information that is material in nature, whether that information has a positive or negative impact on security prices. Moreover, both the United States and the Commission agree that this Court's decision in *Chiarella* v. *United States*, *supra*, 445 U.S. at 230 n.12, which dealt with a market information issue, did not attempt to delineate the outer boundaries of tippee liability. Thus, while tippee liability may arise when a tippee is "a participant after the fact in the insider's breach of a fiduciary duty," such liability also may arise when the tippee, although properly entrusted with confidential information, himself engages in a wrongful misappropriation of that information for his personal advantage. See generally *SEC* v. *Lund*, [1981-1982] Fed. Sec. L. Rep. (CCH) ¶ 98,428 (C.D. Cal. Jan. 22, 1982).

[7] Although *Chiarella* dealt with nondisclosure of "market information" (*id.* at 235), the Court's decision rested on general princi-

a. All nine Justices of this Court agreed in *Chiarella* that there is no "general duty between all participants in market transactions to forgo actions based on material, nonpublic information" (445 U.S. at 233).[8] The Court declined to embrace "such a broad duty * * * absent some explicit evidence of congressional intent." *Ibid.* Instead, the Court adhered to the common law doctrine requiring disclosure only when there is an identifiable "affirmative duty" to divulge information. *Id.* at 228, 231. The majority concluded that such a duty "arises when one party has information 'that the other [party] is entitled to know because of a fiduciary or other similar relation of trust and confidence between them.'" *Id.* at 228; footnote omitted. The majority emphasized that a duty to disclose "arises from the relationship between parties * * * and not merely from one's ability to acquire information because of his position in the market." *Id.* at 231-232 n.14. Thus, an informational advantage is not fraudulent simply because it "gives certain buyers or sellers an unfair advantage over less informed buyers and sellers" (*id.* at 232). The Court noted that "neither

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ples governing all cases of nondisclosure under Section 10(b). See *id.* at 228-230. The Court drew those principles from inside information cases such as *In re Cady, Roberts & Co.*, 40 S.E.C. 907 (1961), as well as market information cases such as *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972). Of course, the summary of case law in *Chiarella* does not purport to be an exhaustive review of legal principles applicable in either inside or market information cases.

[8] See *id.* at 237 (Stevens, J., concurring); *id.* at 235-239 (Brennan, J., concurring); see also *id.* at 239-240 (Burger, C.J., dissenting) ("As a general rule, neither party to an arms'-length business transaction has an obligation to disclose information to the other unless the parties stand in some confidential or fiduciary relation"); *id.* at 252 n.2 (Blackmun, J., dissenting) (recognizing that there is no duty to disclose material nonpublic information obtained through the exercise of "diligence or acumen" and "honest means," as opposed to "stealth").

the Congress nor the Commission ever has adopted a parity-of-information rule" (*id.* at 233).

b. The opinions in *Chiarella* also refer to another ground for imposing a duty to disclose or abstain from trading or tipping. As explained by the Chief Justice in dissent (445 U.S. at 239-245), the common law and the federal securities laws recognize a duty to disclose or abstain whenever the defendant receives material nonpublic information—whether inside information or market information—by misappropriation, conversion, or other tortious conduct. Thus, "a person who has misappropriated nonpublic information has an absolute duty to disclose that information or to refrain from trading." *Id.* at 240. This doctrine condemns informational advantages in securities transactions that are "obtained by conversion and not by legitimate economic activity that society seeks to encourage." *Id.* at 242 n.3. Justice Brennan, in his concurring opinion (*id.* at 239), found this to be a correct statement of the applicable substantive law. Justices Marshall and Blackmun, in dissent, also expressed agreement with the misappropriation theory summarized by the Chief Justice (*id.* at 245-246), and Justice Stevens, while reserving judgment on the issue, characterized the misappropriation doctrine as a "[r]espectable" one (*id.* at 238).[9]

c. The dissenting opinion of Justices Blackmun and Marshall in *Chiarella*, while agreeing that "a relationship of trust can establish a duty to disclose," and that misappropriation or conversion of confidential information for security trading is "dramatic evidence" of fraud, expressed the view that a duty to disclose also should

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[9] Following *Chiarella*, the lower courts have based findings of liability on the misappropriation doctrine articulated by the Chief Justice. See, e.g., *United States* v. *Newman*, 664 F.2d 12 (2d Cir. 1981). The majority opinion in *Chiarella* did not cast doubt on the misappropriation doctrine. Rather, it declined to address it because it "was not submitted to the jury." 445 U.S. at 236; see also *id.* at 243 n.4.

arise whenever an individual has access "to confidential information that the honest investor, no matter how diligently he tried, could not legally obtain." *Id.* at 246-247. This approach would prohibit trading on or tipping of information that is legally unavailable to other investors, while assuring that informational advantages "obtained by honest means reap their full reward." *Id.* at 252 n.2.[10]

In short, the Justices of this Court unanimously have agreed that informational advantages, standing by themselves, do not offend the antifraud provisions of the federal securities laws. Merely characterizing a party as someone with access to material nonpublic information therefore does not suffice to impose a duty to disclose or abstain from trading or tipping, since the "rationale for that limitation is unrelated to the existence of a duty to disclose." *Id.* at 231; footnote omitted. In the present case, both the Commission and the court of appeals failed to analyze the threshold question whether petitioner was subject to a duty to disclose. They simply assumed that because *other persons*—corporate officials with specific employment relationships—were subject to a fiduciary duty to stockholders, that petitioner stood "in their shoes" (Pet. App. B-21 n.42). As *Chiarella* demonstrates, however, a duty to disclose does not arise simply from this kind of verbal characterization.

II. Petitioner Was Not Subject To A Duty To Make General Public Disclosure Of Information Concerning The Equity Funding Fraud Before Passing That Information On To Other Persons

The Commission pretermitted any detailed analysis of the threshold "duty" question because it believed that the present case involved a familiar application of the rule against tipping "inside information" (Pet. App. B-11 to B-12). In fact, however, this case does not. The present

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[10] This broad interpretation was rejected by the majority (see 445 U.S. at 235 n.20).

case involves transmittal of evidence of an ongoing criminal scheme, not inside information of the kind considered in the Commission's past decisions.[11] As we demonstrate below, the nature of this information is vitally relevant to a proper analysis of the question whether petitioner was subject to a duty to make public disclosure before tipping or trading.

1. Initially, the question arises whether petitioner was subject to a duty to disclose or abstain from tipping or trading because he was a "fiduciary" as described in *Chiarella*. If, in fact, he occupied a fiduciary relationship with respect to the shareholders of Equity Funding, then it would be incumbent upon him to make full disclosure and to deal with them with utmost candor, regardless of the nature of the information at issue.[12]

In fact, however, petitioner was not a "fiduciary" with respect to the shareholders of Equity Funding. Unless that term is reduced to a mere conclusory label, the inference is unmistakable that petitioner, like the defendant in *Chiarella*, was a "stranger" to the corporation's shareholders. "He was not their agent, he was not a fiduciary, he was not a person in whom the [investors] had placed their trust and confidence." 445 U.S. at 232-233.[13]

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[11] Accordingly, the disagreement between the United States and the Commission herein relates only to the *extension* of well-established legal principles to the facts of this unusual case. The United States agrees with, and intends to continue to enforce through criminal prosecution where appropriate, the legal requirements established in the Commission's past decisions.

[12] Thus, regardless of the classification of information as inside information, market information, or evidence of crime, a fiduciary would not be permitted to take advantage of uninformed beneficiaries by dealing with them in securities transactions. For example, Ronald Secrist and the other officers and employees of Equity Funding were disabled from profiting at the expense of shareholders without full disclosure. *Chiarella* v. *United States*, *supra*, 445 U.S. at 227-228.

[13] "The horizon is not unlimited * * *. One cannot manufacture a representation for all potential defendants that the public ex-

As Professor Scott has observed, "[a] fiduciary is a person who undertakes to act in the interest of another person." Scott, *The Fiduciary Principle*, 37 Calif. L. Rev. 539, 540 (1949). Ordinarily, "acceptance" of a fiduciary relationship and agreement to act on behalf of the beneficiaries is required to subject a person to fiduciary duties. 1 A. Scott, *The Law of Trusts* 44, 287 (3d ed. 1967); *Restatement (Second) of Agency* § 15 (1958). There is no evidence that petitioner ever agreed to act on behalf of the stockholders of Equity Funding, or that he induced them, directly or indirectly, to place their trust and confidence in him.

A person also may be deemed a constructive fiduciary *ex malefico* when necessary to redress tortious conduct or preserve property rights. Thus, a constructive fiduciary relationship may be implied when unjust enrichment results from misappropriation or improper withholding of property, or when the defendant is guilty of fraud, duress or other similar misconduct. *Restatement of the Law of Restitution* §§ 160, 166 & comments (1937); 5 A. Scott, *supra*, at 3412-3417, 3438-3441; G. Bogert, *The Law of Trusts and Trustees* §§ 471, 482 (2d ed. 1960); *Snepp* v. *United States*, 444 U.S. 507, 515 (1980). More specifically, a person may become a constructive fiduciary if he knowingly acquires "confidential information which is 'owned' by someone else." *Schein* v. *Chasen*, 478 F.2d 817, 823 (2d Cir. 1973). Thus, a "person who, with notice that an agent is thereby violating his duty to his principal, receives confidential information from the agent, may be [deemed] * * * a constructive trustee." *Restatement (Second) of Agency*, *supra*, § 312 comment *c.*; *Restatement of the Law of Restitution*, *supra*, § 201(2)

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pects them to disclose nonpublic information, a relationship of trust and confidence therefore exists, and a duty to disclose is thus implied. Mr. Chiarella would have been held guilty had this approach been applied to printers, but he was not." 5A A. Jacobs, *Litigation and Practice Under Rule 10b-5* 3-433 (2d ed. 1982).

& comment *b*. Accord, III L. Loss, *Securities Regulation* 1450-1451 & n.19 (2d ed. 1961).[14]

As we demonstrate in greater detail below, petitioner is no more a constructive fiduciary *ex malefico* than he is a consensual fiduciary. He did not engage in misappropriation, conversion, or fraud, he did not participate in any breach of fiduciary duty, and he did not obtain confidential information "owned" by someone else. He was not, therefore, a fiduciary *ex malefico* subject to a duty to abstain from trading or tipping prior to the general public announcement of the information in his possession.

2. As the Chief Justice observed in *Chiarella*, *supra*, 445 U.S. at 239-245, a person who misappropriates confidential information may be required to make full disclosure before engaging in a commercial transaction pursuant to traditional doctrines of the law of deceit, which also apply under the federal securities laws. See also Barry, *The Economics of Outside Information and Rule 10b-5*, 129 U. Pa. L. Rev. 1307, 1363-1369 (1981). The facts of the present case, however, clearly show that petitioner did not engage in any form of misappropriation and did not participate in any breach of fiduciary duty.

The Commission's past cases, considering allegations of insider trading, all have involved misappropriation of confidential information. In the seminal case of *Cady, Roberts & Co.*, *supra*, the Commission emphasized that the duty to disclose or abstain from trading or tipping rested on use of "information intended to be available only for a corporate purpose and not for the personal benefit of anyone." 40 S.E.C. at 912. Accord, *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 848 (2d Cir. 1968) (en banc); *Shapiro* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 495 F.2d 228, 232, 237-238 (2d Cir.

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[14] Conversely, a "person who has such information without notice of its confidential nature * * * is not subject to liability for revealing the secret to others." *Restatement (Second) of Agency*, *supra*, § 312 comment c.

1974). See also *In re Van Alstyne, Noel & Co.*, 43 S.E.C. 1080, 1083 & n.3 (1969) (involving "confidential" reports " 'prepared for management use only,' " which were not to be " 'used for public distribution or private gain' "); *In re Blyth & Co.*, 43 S.E.C. 1037, 1039-1040 & n.3 (1969) (involving "confidential" information "intended to be kept non-public until a predetermined time and then disseminated pursuant to established official procedures"); *In re Investors Management Co.*, 44 S.E.C. 633, 640-641 & n.18, 645, 648-651 (1971) (involving confidential information "obtained improperly" by tippees).[15] And finally, in *Chiarella*, this Court likewise characterized inside information as confidential "information intended to be available only for a corporate purpose." 445 U.S. at 227.

In contrast to the information involved in the foregoing cases, the information at issue in this case—evidence of a massive, ongoing criminal scheme—was not "confidential" information available "only for a corporate purpose." Evidence of crime is not the private property of anyone. It is not amenable to "conversion." Those who discover it and spread the news to others are not guilty of misappropriation or theft. Quite to the contrary, any effort to disseminate such information is encouraged by the law, while efforts to preserve its secrecy are strictly forbidden.

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[15] The Commission stated in *Investors Management Co.* (44 S.E.C. at 641 n.18) that there clearly is a duty to disclose or abstain from trading or tipping whenever the recipient of information knows or has reason to know that "the information was obtained by industrial espionage, commercial bribery, or the like," and whenever the recipient comes into possession of "information which [he] has reason to know is intended to be confidential." However, the Commission would "not attach responsibility with respect to information which is obtained by general observation or analysis." See also 44 S.E.C. at 648-651 & n.2 (Commissioner Smith, concurring). Commissioner Smith warned against broader legal interpretations that would "penalize or thwart the quest for new knowledge by analysts and researchers." *Id.* at 649.

As the Commission recognized, Secrist and the other employees of Equity Funding acted properly in disclosing evidence of the Equity Funding fraud to petitioner. "Dirks' informants were entitled to disclose the [Equity Funding] fraud in order to bring it to light and its perpetrators to justice" (Pet. App. B-21 n.42). In the words of the court of appeals, the law has "good reason to" release corporate employees from their duty to keep corporate information confidential when the information concerns corporate crimes or frauds" (Pet. App. A-25). See also *Restatement (Second) of Agency*, *supra*, § 395 comment *f.*: "An agent is privileged to reveal information confidentially acquired by him in the course of his agency in the protection of a superior interest * * *. Thus, if the confidential information is to the effect that the principal is committing or is about to commit a crime, the agent is under no duty not to reveal it." See also *Restatement (Second) of Trusts* § 62 & comments *a.* and *b.* (1959). Beyond this, any attempt to cover up or preserve the confidentiality of evidence of an ongoing crime would be contrary to public policy and a misprision of felony. See *Roberts* v. *United States*, 445 U.S. 552, 557-558 & n.5 (1980), noting that "[c]oncealment of crime has been condemned throughout our history," and that affirmative efforts to preserve the secrecy of a criminal conspiracy constitute a violation of 18 U.S.C. 4. Accordingly, there is no basis whatsoever for viewing the revelations of Secrist and the other Equity Funding employees as an improper disclosure of "confidential" information or a breach of fiduciary duty, and petitioner cannot be characterized "as a participant after the fact in the insider's breach of a fiduciary duty" (*Chiarella* v. *United States*, *supra*, 445 U.S. at 230 n.12).

Nor can petitioner's use of the information, after it was divulged to him, be viewed as any type of misappropriation or conversion. Because evidence of crime is not anyone's private property, and because public policy favors its unfettered dissemination, it is doubtful whether

restrictions could be placed on petitioner in communicating it to other persons. In any event, the record establishes unequivocally that petitioner used the information in precisely the manner intended by his informants—to set up the "hue and cry" (*Roberts* v. *United States*, *supra*, 445 U.S. at 557). Secrist, who originally provided the information and monitored its use, intended petitioner to divulge the information to institutional traders who would precipitate large-scale market activity, and thereby hasten the investigation and termination of the fraud (see page 3, *infra*). Secrist also gave his permission to convey the information to the *Wall Street Journal* (*ibid.*). Petitioner's communications with the auditors (see *id.* at 4-5) further advanced Secrist's stated objective of exposing the fraud. And, precisely as Secrist anticipated, petitioner's activities quickly achieved the desired objective while regulatory authorities lagged behind. Far from inflicting a tortious injury on the corporation, petitioner's actions served to expose and terminate corrupt wrongdoing by some of its highest ranking officials.

In short, there is virtually no basis for suggesting that petitioner engaged in misappropriation or other tortious conduct that would impose upon him a duty to guarantee disclosure to the public at large before disseminating information about the Equity Funding scandal.[16]

3. Finally, it is significant to note that, even under the broadest formulation of the "abstain or disclose" doctrine articulated in the *Chiarella* case, petitioner still is immune from liability. The dissenting opinion of Justices

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[16] In other situations, a question may arise whether a recipient of information has obtained evidence disclosing criminal conduct as opposed to mere "bad news" which, in certain limited circumstances, is properly treated as confidential by a corporation. See note 24, *infra*. The test, in such cases, is whether the recipient "know[s]" or "has reason to know" that the information is "confidential" corporate information, rather than evidence of a crime—which is subject to no legitimate expectation of secrecy. See *In re Investors Management Co.*, *supra*, 44 S.E.C. at 641 & n.18, 650 & n.2.

Blackmun and Marshall would prohibit trading on or tipping of "confidential material information that is not legally available to others," while permitting unrestricted use of information gotten through superior "diligence," "acumen," and "honest means" (445 U.S. at 251, 252 n.2). The evidence of crime at issue in this case was not withheld from members of the general public by force of law; petitioner acquired it solely through diligence, acumen, and honest means. Other analysts interested in investigating Equity Funding's operations were free to contact its former employees, several of whom made attempts to expose the fraud (Pet. App. A-9 to A-10 n.6; J.A. 15-16, 22-23, 36-37, 66-67, 96-97, 229). The fraudulent scheme was frequently discussed by company personnel, many of whom freely conferred with petitioner (Pet. App. B-9; J.A. 34, 36, 39-40, 234-236, 239-242, 257);[17] they expressed relief when it was inquired into (J.A. 241); and they demonstrated their willingness to confer with persons other than petitioner, including journalists, analysts, investors, and government officials (J.A. 17-18, 35, 39-40, 50-51, 131, 201-202, 213, 226, 235, 246, 259, 270). Petitioner obtained the information in question through a combination of good fortune and diligent investigative technique, and in a free enterprise economy "advantages obtained by honest means" are entitled to "reap their full reward" (*Chiarella* v. *United States*, *supra*, 445 U.S. at 252 n.2). See Brudney, *supra*, 93 Harv. L. Rev. at 360-361, 365; see also Lorie, *Insider Trading: Rule 10b-5, Disclosure, and Corporate Privacy: A Comment*, 9 J. Legal Stud. 819, 821 (1980) ("in the *Equity Funding* case, the information was secured by the private initiative of someone who

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[17] "[I]t was common knowledge, all this, what he was telling me, * * * it was common knowledge around the water cooler where everybody talked about it" (J.A. 34).

enjoyed no privileged position with respect to access to information").[18]

III. Penalizing Petitioner For His Actions Will Undermine The Effectiveness Of Federal Law Enforcement And Impair The Policies Underlying The Prohibition Against Insider Trading

As Judge Wright observed (Pet. App. A-3), "[l]argely thanks to Dirks one of the most infamous frauds in recent memory was uncovered and exposed," while governmental authorities "repeatedly missed opportunities to investigate Equity Funding." The Commission also acknowledged petitioner's "important role in bringing [Equity Funding's] massive fraud to light" (*id.* at B-26), but concluded that its censure order would not "chill" other analysts in the "investigation of rumors" of similar corporate frauds (*id.* at B-25). We are not so sanguine about the impact of the Commission's order on the private investigation of corporate crime.[19]

1. Petitioner's reputation as a competent security analyst caused Secrist to approach him (J.A. 19-20), even though Secrist was reluctant to communicate with government authorities (*id.* at 15-16, 22, 36-37, 66-67). Petitioner spent several weeks investigating Secrist's allegations—on his own time, at his own expense, and despite substantial personal danger. The direct result of his investigation was that the price of Equity Funding stock fell dramatically, trading was suspended, and government authorities ultimately took remedial action. As the principal architect of the Equity Funding fraud con-

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[18] Petitioner did not himself make any stock trades on the basis of the information he received (J.A. 154). His business reputation and the commercial interests of his firm, however, apparently were advanced by his investigative activities (Pet. App. B-6 to B-7).

[19] The prohibition announced in the Commission's opinion is backed not only by administrative sanctions, but also by potentially "Draconian" civil liabilities (*Shapiro* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, *supra*, 495 F.2d at 242).

ceded, petitioner deserves "personal credit" for uncovering it (J.A. 115). Had petitioner not taken action, the illegal scheme, which lasted for nearly a decade, could have persisted for an additional period of time—causing even greater injury to the public (J.A. 64, 116-117).[20]

If the Commission's decision is allowed to stand, few analysts, brokers, or other securities professionals who hear rumors of corporate crime can be expected to follow a similar course. Investigative efforts are costly, and if private parties who are in the business of ferreting out and analyzing information are not allowed to trade with or even transmit their findings until the information is fully disclosed to the public at large, they will have no reason to undertake their investigation at all.[21] While, of course, the Commission has not prohibited analysts from exploring public records to substantiate rumors of criminal conduct, few corporate conspiracies can be uncovered without obtaining information from an inside source. The Commission's approach, therefore, is certain to reduce, and may well eliminate, the role of securities professionals in detecting and analyzing major corporate crimes.[22]

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[20] Surprisingly, the Commission's opinion attempts to minimize the extent of petitioner's investigative work (Pet. App. B-18). In our view, the record fully supports the court of appeals' conclusion that petitioner served as a highly effective private "detective" (Pet. App. A-3), obtaining corroboration of facts upon which government authorities were unable to take prompt action. See Testimony of Stanley Sporkin, C.A. App. 1076: "We were really in a quandry, on the week of March 26, about what we should do. We had no real verification of the facts." See also Pet. App. A-9 to A-10 n.6; J.A. 273.

[21] See Easterbrook, *Insider Trading, Secret Agents, Evidentiary Privileges, and the Production of Information*, 1981 Sup. Ct. Rev. 309, 337 ("Dirks's efforts were costly. * * * The ability to pass secret information to clients enabled Dirks to profit from his investigation, which redounded to everyone's benefit.").

[22] See Scott, *Insider Trading: Rule 10b-5, Disclosure and Corporate Privacy*, 9 J. Legal Stud. 801, 818 (1980) ("the SEC's Equity Funding position is [an unintended] boon to the successful commis-

In our view, such a result would have a significant adverse effect on federal law enforcement. The resources available to government law enforcement agencies are limited, and private parties with a financial incentive to pursue evidence of wrongdoing provide a valuable supplement (see Pet. App. A-25 to A-26).[23] That is particularly true in the securities industry, where analysts have the expertise and resources to investigate rumors, and a strong incentive to arrive at the truth about alleged corporate wrongdoing.

2. As the Commission correctly observed (Pet. App. B-12 to B-13; footnote omitted), "market efficiency in pricing is significantly enhanced by [the analyst's] initiatives to ferret out and analyze information, and thus the analyst's work redounds to the benefit of all investors." Until the Equity Funding fraud was exposed, as the Commission stated in its Brief in Opposition, "the information in the market in which the company's securities had been trading was grossly inaccurate" (*id.* at 2).

Market efficiency is not, of course, an excuse for insider trading, as the Commission has explained (Pet. App. B-13). It cannot justify an insider's misappropriation of confidential information, available only for a bona fide corporate purpose. Such conduct not only harms the corporation, but also violates the insider's fiduciary duty to shareholders, and ultimately impairs investor confidence in the public securities markets. See *In re Faberge, Inc.*, 45 S.E.C. 249, 254 (1973). Market efficiency need not depend upon insider trading because corporations, acting

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sion and prolongation of corporate fraud"). Accord, Easterbrook, *supra*, 1981 Sup. Ct. Rev. at 337 ("Dirks did everyone a service. The sooner frauds are discovered—and the more costs a defrauder bears in deferring disclosure—the fewer frauds there will be.").

[23] This point is a familiar one to the SEC. See, e.g., *J.I. Case Co.* v. *Borak*, 377 U.S. 426, 432 (1964).

in compliance with the law, are required to promptly divulge all material facts that are relevant to investors.[24]

The situation is quite different, however, when the information in question is not confidential corporate information, subject to periodic disclosure requirements, but evidence of an ongoing criminal conspiracy involving those who control the company. Such information will never become public through the Commission's mandatory disclosure requirements: it will be reflected in the market price of securities only if someone conducts an effective investigation, precisely as petitioner did.

3. Considerations of fairness to investors, and the need to preserve investor confidence in the public securities markets, while strongly supporting the traditional rule against insider trading and tipping, provide no support for the Commission's decision here.

The Commission's decision in this case threatens to undermine, rather than enhance, investor confidence. If administrative rulings strip away the incentive of security analysts to investigate frauds, there will be more frauds in the future and they will persist for longer periods of time. By contrast, if investors may continue to expect that competent analysts, acting in their own economic interest, will assist the government in policing the securities markets, their reliance on the integrity of the marketplace will be strengthened.

Finally, no consideration of fairness requires the result reached by the Commission. Petitioner, unlike the defendants in traditional insider trading cases, did not misappropriate information, did not violate any fiduciary duty to stockholders, and did not exploit any privileged

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[24] Prompt disclosure is required by the SEC's periodic disclosure rules, as well as the rules of the exchanges on which the corporation's securities are traded. See II L. Loss, *Securities Regulation* 805, 809-823 (2d ed. 1961). See especially SEC Release No. 34-8995, *Timely Disclosure of Material Corporate Developments*, 35 Fed. Reg. 16733 (1970), reproduced in 2 Fed. Sec. L. Rep (CCH) ¶ 23,120A; see also *id.* at ¶ 23,121.

access "to confidential information that the honest investor, no matter how diligently he tried, could not legally obtain" (*Chiarella, supra*, 445 U.S. at 247 (Blackmun, J., dissenting)). Instead, he obtained his information through honest and costly investigation, and few—if any—investors would believe it unfair for him to profit thereby.

It was inevitable that the Equity Funding fraud would have victims. Because of petitioner's actions leading to the discovery of the fraud, there were fewer victims than there otherwise would have been (J.A. 64, 116-117). And to the extent that private parties retain an incentive to act as petitioner acted, there are likely to be fewer victims of such frauds in the future.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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DECEMBER 1982

☆ U. S. GOVERNMENT PRINTING OFFICE: 1982 395074 1225